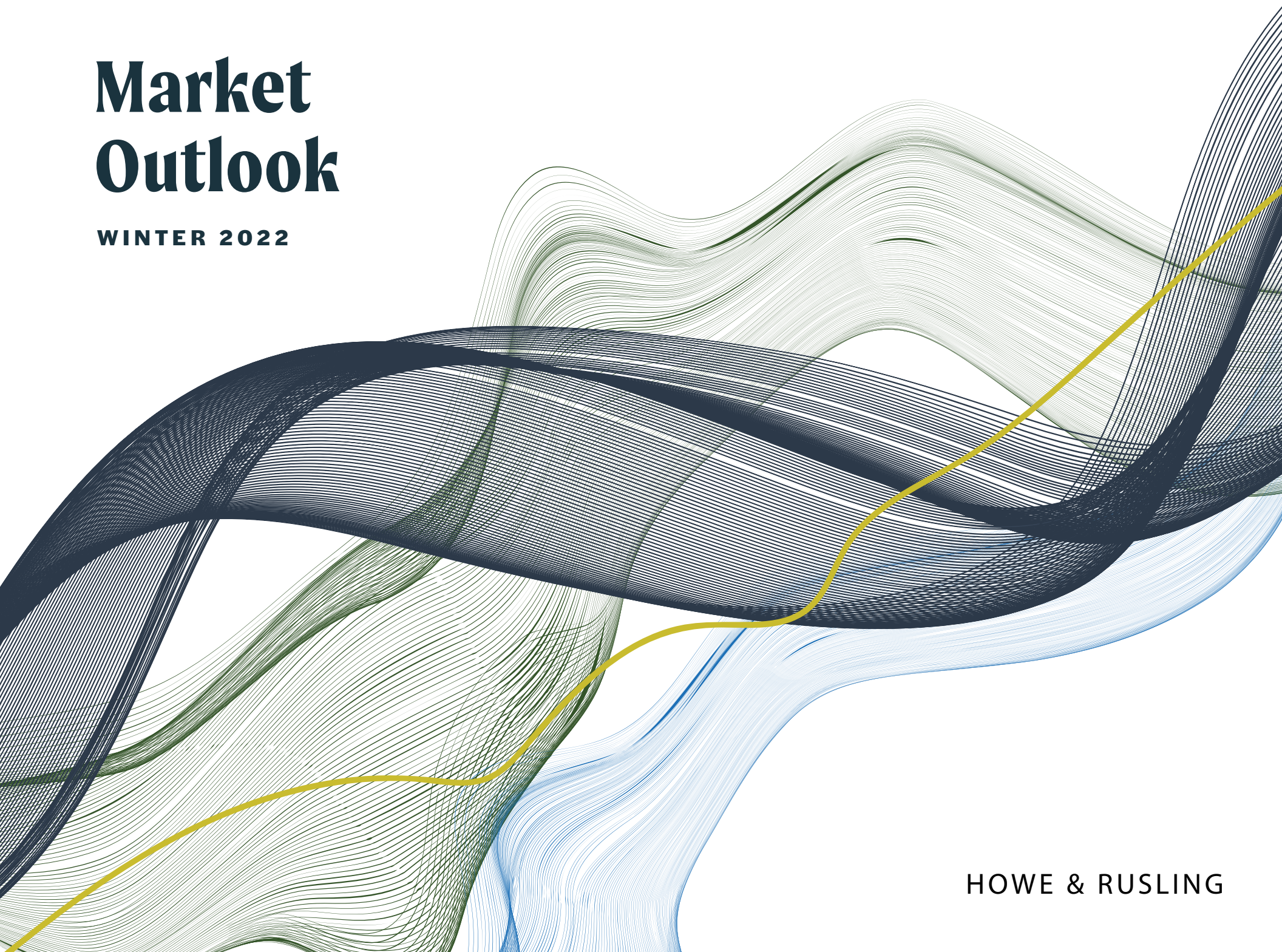


Market Outlook

WINTER 2022



HOWE & RUSLING

On Our Minds

If we recall a year ago, everyone, worldwide, was beckoning the New Year with wide-open arms and looking forward to putting the prior year behind – all because of the pandemic. Dare I say déjà vu. Perhaps this new year will be the end of the pandemic, perhaps. While we are wealth advisors, constantly interpreting current and historical market data, coupled with current events, the pandemic proved to be the variable of all variables.

However, 2,700 years ago, the Greek Philosopher Heraclitus coined the phrase, “the only constant is change.” In today’s terms – life goes on.

Despite the chaos of a pandemic, risk markets performed remarkably well over the last two years of turmoil. Like we’ve written numerous times, the markets move principally on two things: interest rates and earnings. Therefore, while the past two years have been hard on our daily lives, interest rates remained very low, supporting favorable market returns. Also, given the unpredictability of the pandemic, most earnings expectations were extremely low, setting the bar low to outperform. In retrospect,

it’s been a very good time to be an investor, and the reason we had an equity overweight in our allocations during all of 2021 (and the tail end of 2020).

On our minds for early 2022 are several things – the pandemic, interest rates, and inflation. These will all be critical, near-term influences on the markets. We will address each in this Outlook.

Throughout our Outlook we will share a few charts which help shape our perspective on the economy and ultimately inform our investment decisions. Regardless of any déjà vu feeling we might have, repeating the past truly never happens, so it is critical to embrace the teachings of Heraclitus and know change is the only constant.

On behalf of our Macroeconomic Team, we hope you enjoy our 2022 Winter Market Outlook, and we wish you a Happy and Healthy New Year.



GREGORY T. FARRELL

Vice President, Senior Wealth Manager,
& Macroeconomic Team Chair



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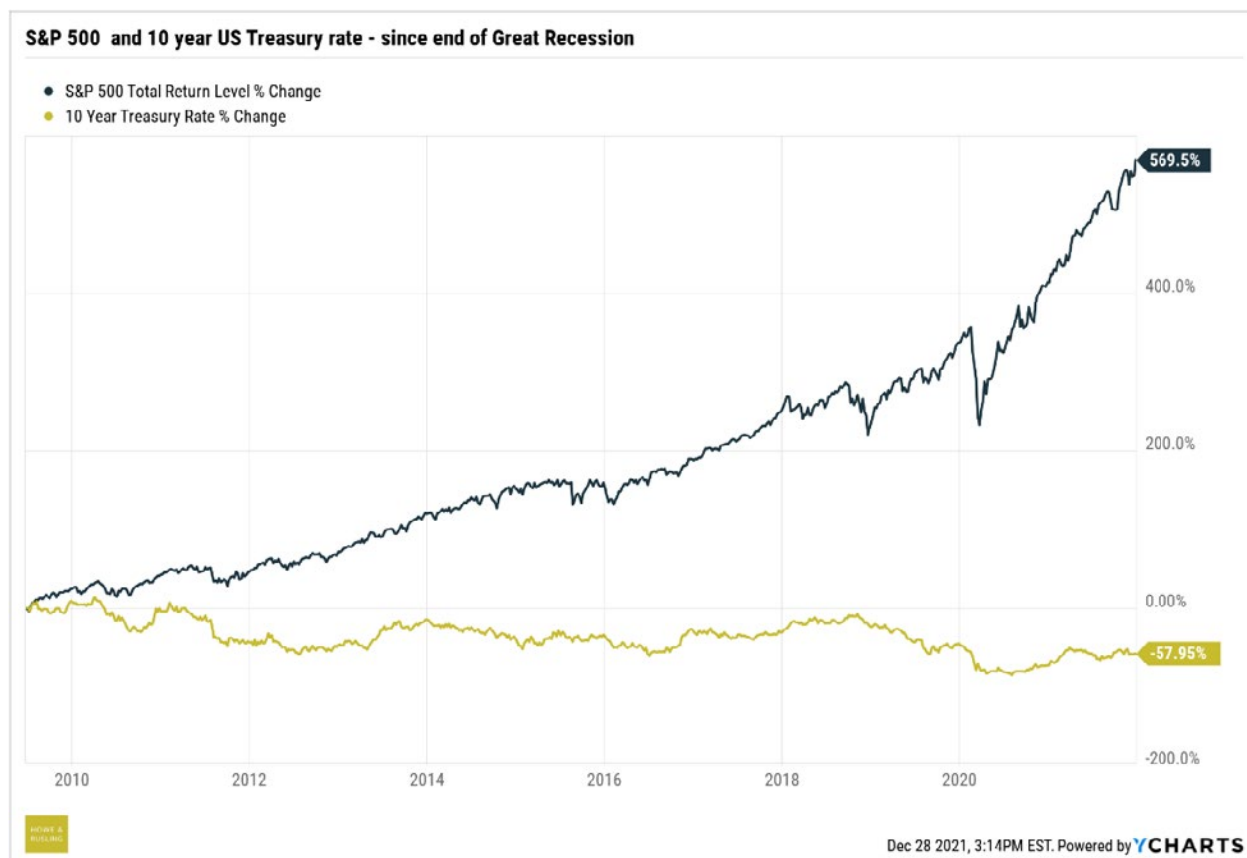


Our Core Signals

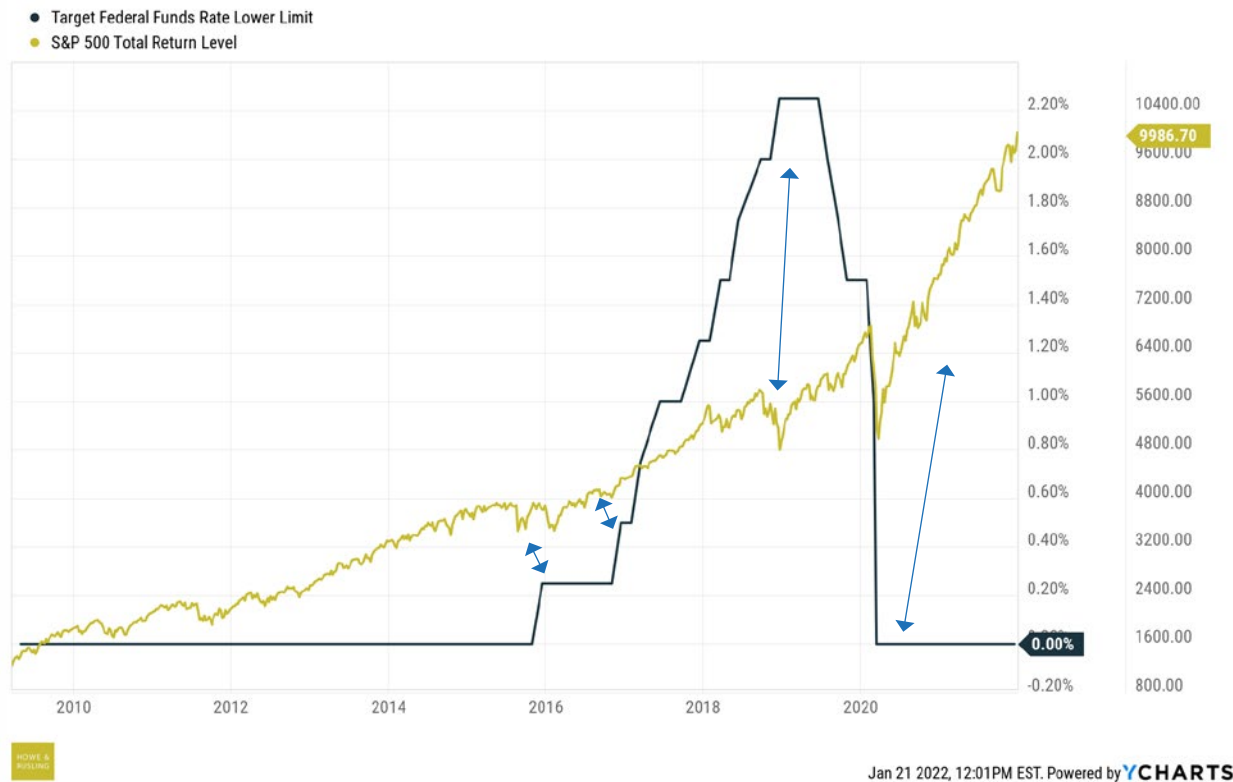
FIXED INCOME

As we said in our preface, interest rates (and earnings), move markets.

The low rates after the Great Financial Crisis (and again after the onset of the pandemic), have contributed to strong market returns, as exhibited by a declining 10-year Treasury rate and subsequently rising S&P 500.



S&P 500 and Federal Funds rate since end of Great Financial Crisis

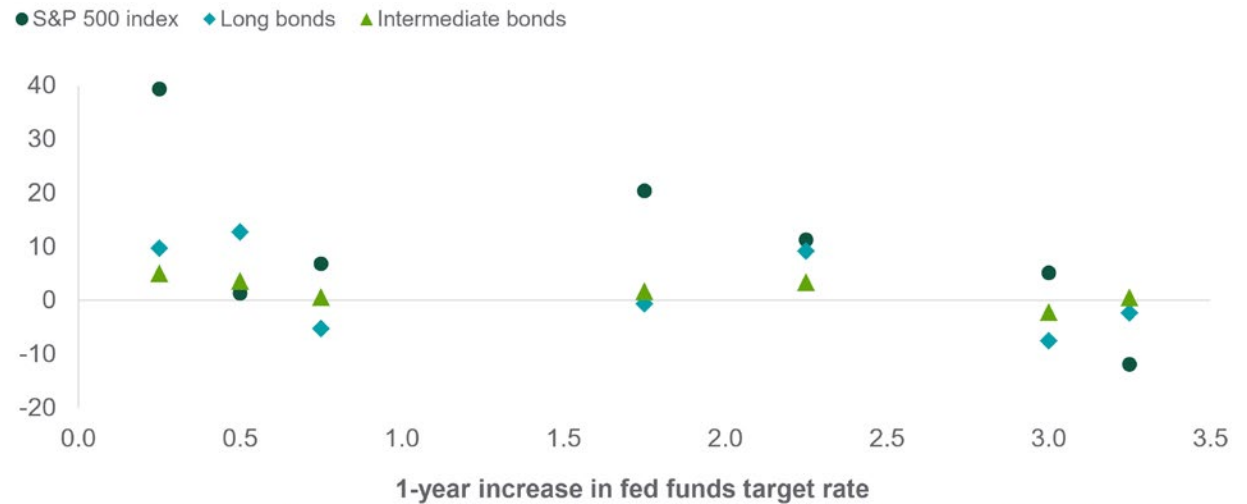


While the 10-year Treasury is a market proxy for all interest rates, the Fed has suppressed short-term rates by lowering the Federal Funds rate to zero and buying bonds (which suppresses supply and keeps rates low). When the Fed Funds rate rises (in chart to the left), there tends to be a direct impact on the market.

Rates do impact the equity markets, which is why we vigilantly monitor all rate movement. Given the strength of the risk markets, an economy with more jobs than willing workers, and rising inflation, the Federal Reserve finally has disclosed its intent to raise rates. While this was not a surprise at first, the notes from the Federal Reserve meeting of December 2021 revealed a more hawkish tendency than the market anticipated, with perhaps 4 rate hikes in 2022. We will discuss further, but while markets might react negatively at first, actions eventually speak louder than words.

To the right are real-life scenarios of the effect on various asset classes after the Fed makes an initial rate hike.

TOTAL RETURNS 6-MONTHS BEFORE THROUGH 6-MONTHS AFTER INITIAL RATE HIKES



Source: Northern Trust Asset Management, Bloomberg. Long bonds: Bloomberg U.S. Long Government/Credit Index; Intermediate bonds: Bloomberg Barclays Intermediate U.S. Government/Credit Index. Data through 11/30/2021. It is not possible to invest directly in any index.



As we examine rate movements, throughout history the 10-2 spread (the difference between the 10-year Treasury and the 2-year Treasury) has served as a reliable indicator for the economy and the markets. Whenever the spread shrinks (known as a flattening yield curve), it raises concern for unfavorable forthcoming economic conditions (such as a recession). Historically when the 10-2 spread drops below 0% (known as an inverted yield curve), a recession has followed.

In absolute terms, the spread has been shrinking over the past few months and is in the 0.80% range. While there has been subsequent movement (up) in the 10-year Treasury, 80 basis points does not allow a lot of room for the Federal Reserve to have a heavy hand in raising rates.

THIS IS IMPORTANT, as when the Federal Reserve raises rates, it is done on the shorter end of the maturity curve, causing the 2-year yield to rise faster than the 10-year (which typically flattens the curve). Hence, while the market consensus is rates will increase, we likewise believe the Fed will be carefully monitoring the spread, so as not to toss the economy into a tailspin. Therefore, while the Fed has pressure on them to corral inflation, actions will speak louder than words.

If rates go up, as anticipated, the value of bonds drop. However, rate movement is never a guarantee, given continued variables such as the pandemic, and political risk occurrences (domestic and foreign), which impact all market investments. That said, despite the occasional swing, the asset class (fixed income) is known for its consistent return (chart to the right) with average sways in the low single digits, versus double digit swings of equity holdings. So, despite value fluctuations from rate changes, the asset class is still an important part in any portfolio.

STRATEGY

While rates move up and down, the fixed income asset class is a key component of any portfolio providing stability, and needed cash flow, during volatile times.



INFLATION

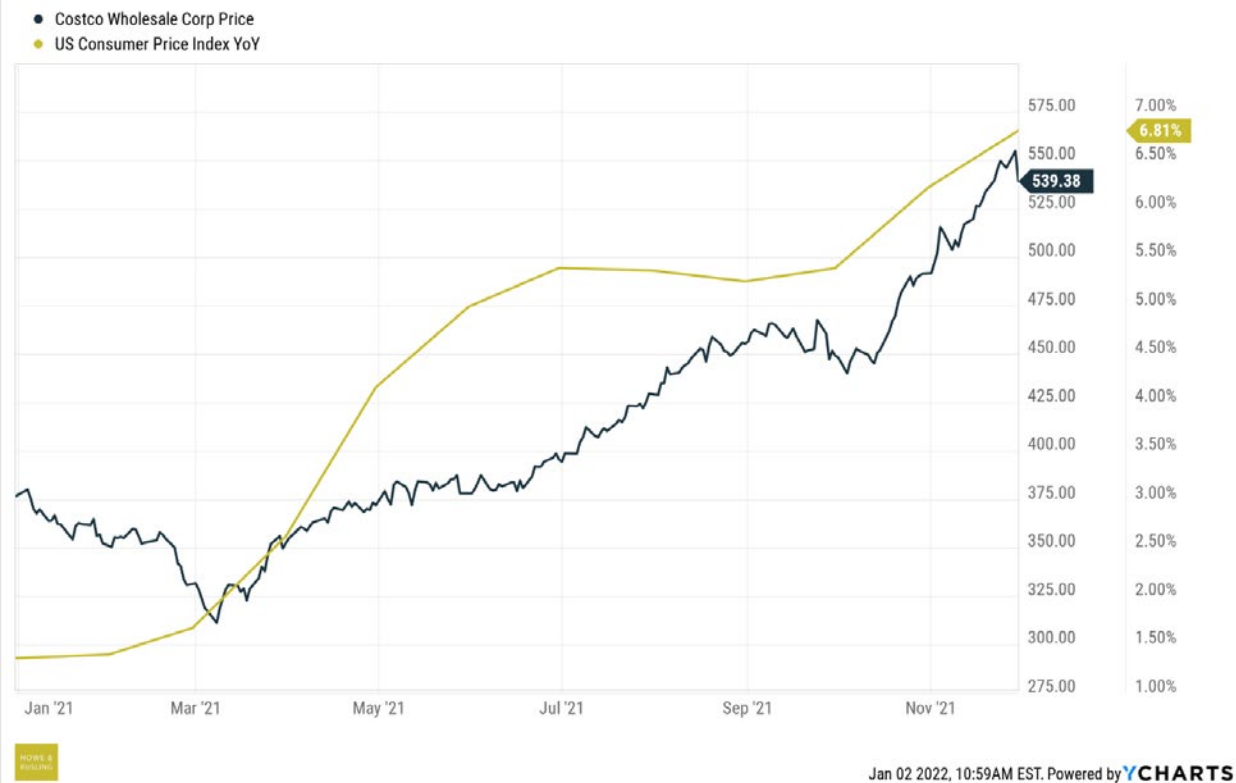
How long will inflationary pressures persist? If history is to be our guide, we do have analogous periods to illuminate how it will end. How do we know? We have the Federal Reserve, who can dramatically dampen demand by aggressively raising rates. As the old saying goes, “a bull market never ends, it gets wiped out by the Fed.”

With inflation numbers coming to the forefront in April 2021, with a reading above 4% for the first time in decades, one thing we know for sure is consumers are a crafty bunch, and they will not let inflation get in their way of satisfying their desire for goods.

A great way to look at inflation, and buying habits, is to look at Costco (COST) over the course of 2021. As inflation started to come into focus in April 2021, Costco started to increase in value.

We use Costco to illustrate the effects of inflation as it shows how consumers looked to stretch their dollar. We also show it as an example of owning the right stocks during inflationary periods. Costco clearly was a winner.

Rising Prices and Discount Retailer Costco



Looking at CPI since 1982, we can see several big spikes, notably in the early 80s, 90s, as well the Great Financial Crisis. Obviously, we are experiencing a sizable spike at present.

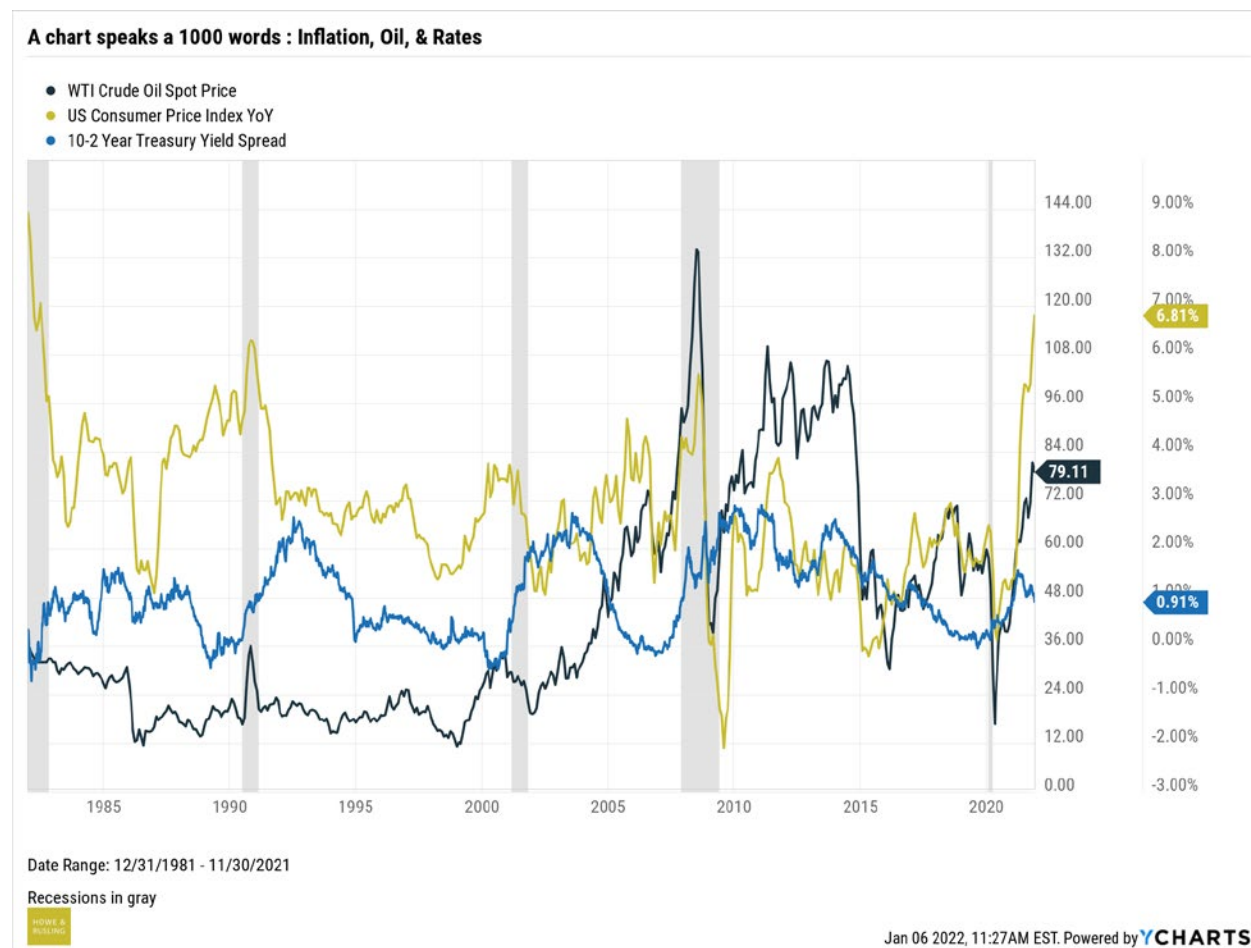
While we can elaborate with lots of words, our chart can do the talking. Look at the gold color line (historical inflation as measured by CPI) compared to the black line (the price of oil as

measured by West Texas Intermediate Crude price); they move in the same way at the same times. Therefore, inflation in a nutshell seems to say that as West Texas goes, so goes inflation.

The blue line is the previously discussed 10-2 Treasury spread, which we will use as proxy for the Fed controlling rates to combat inflation. While there is a lag, inflation (gold line) does drop as the blue line drops, with the inflation dropping at a faster clip.

Granted, the proverbial “this time is different” has been said a lot, given the impacts of a pandemic-induced worldwide shutdown. However, the chart speaks loudly, and history is saying the path forward might have some challenges.

While this might instill some fear in market participants, the positive news is the US was a net exporter of crude in 2020, which can help with inflationary pressures.



At least historically, the price of oil can be seen as a proxy for inflation. If we continue with safe exploration and production domestically, and therefore lessen our reliance on imported oil, for now, this can change inflationary pressures. As we continue to move to other fuel sources, there will eventually be another proxy for inflation, but for now, the solution to our current inflation might in fact lie in a West Texas oil field.

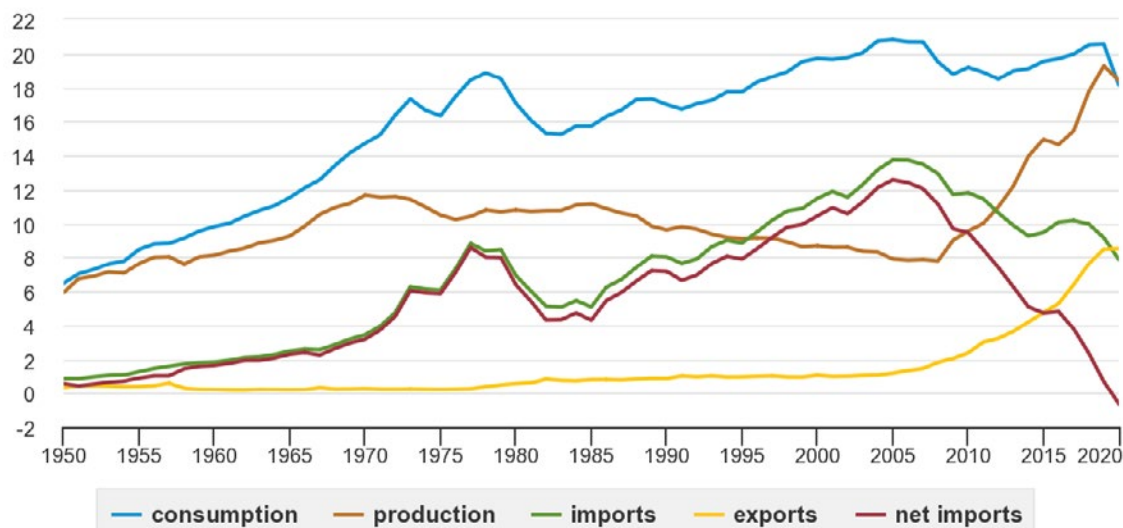
While oil is very important, we are anticipating a moderation in the YoY inflation numbers, given some return to “normalcy,” as indicated with the below frequency data. Activity in most categories has returned to “semi-normal” levels. This should relieve some of the extraordinary demand pressures.

STRATEGY

This too shall pass. Holding companies that have the potential for earning gains from either inflationary price increases or from cyclical sales, are an inflation hedge.

U.S. petroleum consumption, production, imports, exports, and net imports, 1950-2020

million barrels per day



Source: U.S. Energy Information Administration, *Monthly Energy Review*, Table 3.1, March 2021, preliminary data for 2020

WEEKLY HIGH FREQUENCY DATA

Indicator	Date (2021)	Level	2019 Level	% Change 2019	% Change MOM	% Change WOW
Initial Jobless Claims	December 24	198,000	218,000	-9.2%	-12.8%	-3.9%
Continuing Jobless Claims	December 17	1,716,000	1,725,000	-0.5%	-12.2%	-7.5%
ASA Staffing Index ¹	December 20	105.6	94.1	12.3%	-2.8%	-2.1%
Weekly Retail Sales ²	December 25	21.4%	7.8%	NA	NA	NA
Box Office Receipts	December 17-23	\$450,352,692	\$485,547,943	-7.2%	203.6%	659.1%
Rail Car Traffic (cars)	December 24	420,373	373,617	12.5%	-2.4%	-16.6%
Steel Production (net tons)	December 27	1,802	1,876	-3.9%	-1.9%	-0.2%
Hotel Occupancy	December 12-18	53.8%	50.0%	7.6%	-9.9%	-6.3%
OpenTable State of the Restaurant Industry ^{3,4}	December 28	NA	NA	-23.2%	-19.1%	-6.8%
TSA Checkpoint Data ³	December 28	1,952,511	2,371,516	-17.7%	-5.2%	-4.4%
Supply of Motor Gasoline in the US (Mbbl/d)	December 24	9,724	8,961	8.5%	10.6%	8.2%
Global Commercial Flights ⁵	December 29	87,301	107,679	-18.9%	-3.5%	-9.0%

Level is at a new recovery best

Source: First Trust Advisors, Bloomberg, Department of Labor, Redbook Research, Box Office Mojo, Association of American Railroads, American Iron and Steel Institute, Hotel News Now, OpenTable, Transportation Security Administration, Energy Information Administration, American Staffing Association, Flight Radar 24

2019 Level and % Change 2019 are from the same week in 2019, unless otherwise noted. MOM = Month-over-Month; WOW = Week-over-Week.

VALUATIONS

In any given client call, the topic of **an overvalued market** is a common concern.

When we look at markets, moving averages can be a good technical indicator of future market movements, implying whether a market might be over, or undervalued.

As can be seen in the below 5-year historical chart, **the S&P 500 is presently above both its 200-day, and 50-day, moving averages – which is a positive indicator.**

The 200-day moving average is a strategic indicator, while the 50-day moving average can be used both tactically (to buy and sell in selected time periods) and can be used as a potential early indicator of future stress or opportunity.

At present, the 200-day average is firmly in good standing, with a good spread from the current S&P level. Whenever the 200-day level drops below the current S&P

S&P 500: 200 & 50 Day moving average s- 5 year history



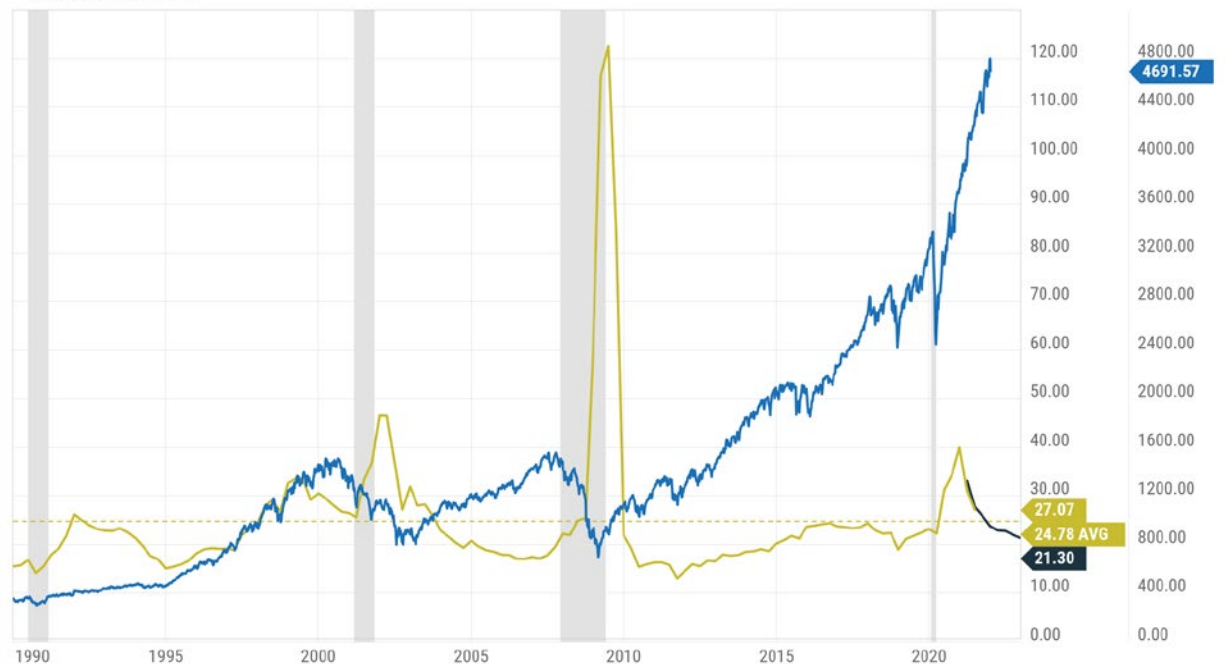
price level, it usually does not end well, with the end of 2018 and the 2020 pandemic as glaring examples.

In reference to the 2018 incident, this principally can be attributed to 'missteps' by the Federal Reserve in raising rates. These hikes happened during the first year of Jerome Powell serving as

Federal Reserve Chair. Since then, we believe Chairman Powell has seen the effects of his words, and actions, and to that point we also believe he and his committee include the stock market in their overall view of the economy, even though they publicly do not comment about the markets. They know the importance of the markets to the economy.

Price Earnings Ratios for S&P 500

- S&P 500 P/E Ratio Forward Estimate ()
- S&P 500 P/E Ratio ()
- S&P 500 Level (USD)



Date Range: 12/29/1989 - 12/31/2022

Jan 07 2022, 12:06PM EST. Powered by YCHARTS

Another measure of valuation is the forward price-earnings ratio. This measures the current price of a stock against its estimated future earnings per share. A lower-than-average ratio could be a buying opportunity, while higher than average ratios could be a cautionary signal.

Looking at 2021 year-end, the long-term average P/E of the S&P was 24.78, while the forward 2022Q3 P/E is estimated to be 21.30, below the average. While opportunity, and risk, constantly exist when investing, a shrinking forward price might be seen as an opportunity for value. However, as can be seen from the chart, there is not a clear-cut correlation of P/E ratios to future market performance. While many profess the P/E ratio as a good indicator of value, it is a rear-view mirror look, and like present, gets extremely exaggerated during times of stress (as seen around recessionary periods).

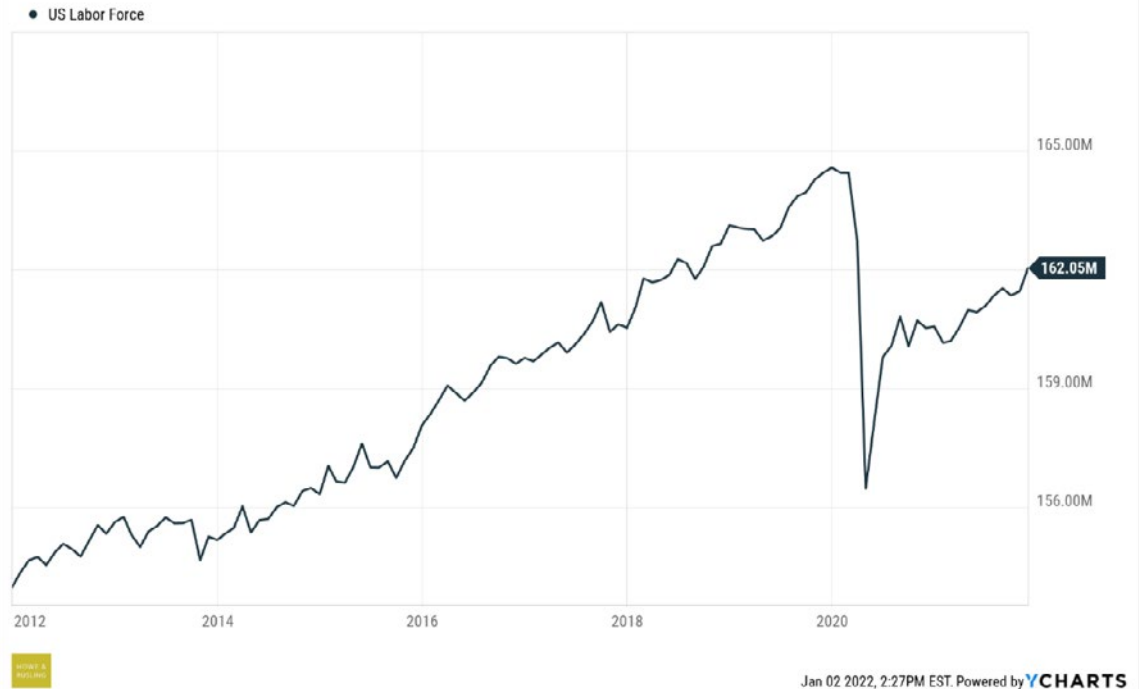
PANDEMIC INFLUENCE

The pandemic has had a way of throwing curve balls at traditional forecasting. Let's take labor as an example.

While it was easy to understand high unemployment from the Great Shutdown, not many forecasts included "the Great Resignation." The assumption was when doors opened again, employees would return to work. That has not fully been the case, which has put pressure on labor supply.

Complicating the labor pool is fewer immigrated workers, either from continued travel and border issues, or their vaccines are not of the approved variety by the US government. Less workers, during a non-recession period, means higher wages (which has potential inflation implications). Until the pandemic settles, it will be hard to forecast how many employees may eventually return to the labor force. We continue to monitor.

10 Year History of US Labor Force



Furthermore, impacting the labor picture is the near-term pressure on employers of sick-related leave (versus unemployment claims). Hopefully by the time this is put to press, the Omicron surge will have peaked, and employees can resume work. However, at year-end 2021, the pressure was real. We believe this is a temporary setback, but the pandemic has been a series of temporary setbacks.

While we could go on with other pandemic related variables (like housing, meme stocks, or yet to be determined issues), the above labor example exemplify the challenge the pandemic has had on economic forecasting, and more importantly, the markets. We continue to take each day's news with measured interpretation.



STRATEGY Gather facts, determine trends, and invest cautiously knowing trends change.

Our Vision



The past year was not what everyone expected. We all entered 2021 with hopes of putting the pandemic behind us and moving forward. Alas, that was not fully the case, and here we are again, hoping for a better future.

We cannot alter the past (or for that matter the future), but we can use the information given to us to make reasonable assumptions.

We envision the pandemic enduring, but over the balance of 2022, becoming more of an annual “flu” than an outright virus with many at risk. Obviously, we are in different times, but fortunately, from present science, we are seeing the current variation of the virus (Omicron) is not as deadly as the first waves, especially when no vaccine was available during the first variant. As the virus continues to change its structure,

science tells us it will eventually be an annual concern, just like the flu. With that, the world will adapt, and individuals will make their own decisions on the risk.

We believe the future is bright, but we also have learned a lot in the past two years, which has made us better wealth managers. While we had a short-lived recession, we have seen many investment opportunities, and traps, as the pandemic has thrown us curve balls. We are stronger as managers (and as a world) from all we have experienced in the past two years. Our vision is relatively clear – use the past to move forward, use the patterns we have learned exist, and do not be complacent. Instead, interpret and adjust, and remember change is the only constant.

Macro Team

QUESTIONS



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